In contrast, the non-recurring studies are designed to identify the specific activities involved in provisioning CLEC requests, and then estimating the labor costs involved in performing those activities, levelized over the planning period. Forward-looking adjustments are made to take into account developments that should eliminate or reduce the need for (or time involved in) performing specific activities.

II. DEVELOPMENT OF FACTORS

Factors are utilized by Verizon to estimate costs that will be required to provide a UNE based upon a relationship that is developed from real, current data. Factors have been divided, for the purposes of this discussion, into (A) investment loadings; (B) expense-related; and (C) capital-related annual cost factors.

A. INVESTMENT LOADINGS

All of the investments used in Verizon's cost studies reflect the total installed investment (also called total cost installed (TCI)) of the necessary facilities and equipment, including required support investment. Verizon uses investment loading factors to translate the materials-only price of an asset ("material-only investment") into the TCI for that asset. Specifically, Verizon has developed Engineer, Furnish & Install (EF&I), Land and Building (L&B), and Power factors to calculate the TCI for assets in the digital switching, digital circuit and originating/terminating plant accounts.

1. Engineer, Furnish & Install Factors

The EF&I factors help translate a material-only investment into an installed investment by accounting for items such as vendor engineering, Verizon engineering,

transportation, warehousing, hoisting, vendor installation, Verizon installation and acceptance testing or other plant labor, and interest during construction. The factors represent the relationship between these items and base year material-only investment.

EF&I factors are developed on a regional basis, to account for the fact that there may be relatively large variations from year to year in the amount of a given class of equipment being placed in any individual jurisdiction. The data used in developing the EF&I factors is found in Verizon's Detailed Continuing Property Record (DCPR) database.

2. Land & Building Factors

The Land and Building (L&B) factors identify the land and building investment that is required to support equipment classified to central office equipment accounts. The L&B factors are appropriately applied to equipment classified as operator systems, digital circuit equipment, and digital switch. These factors are developed on a state-specific basis, reflecting the land and building investment associated with the central office equipment investments in the relevant state.

3. Power Factors

The Power factors represent a relationship between the investment in power equipment necessary to run the installed equipment and facilities and the installed investment in the equipment itself. Separate factors are developed by class of equipment. For the same reasons applicable to the EF&I factors, Power factors are also developed on a regional basis.

B. EXPENSE-RELATED ANNUAL COST FACTORS

Annual Cost Factors (ACFs) are used to translate TCI into annual costs for UNEs; they also are used to develop the final non-recurring costs from the identified labor expenses related to the provisioning of UNEs. ACFs are developed as ratios that represent relationships between a subset of costs and (1) their associated plant account investments, (2) relevant expenses, or (3) total revenues.

In the case of expense-to-investment ACFs, the costs that are incurred for specific plant accounts are directly attributed only to investments in those accounts, while costs that are not specific to a plant account are spread equally across all affected revenue-producing investments. This approach ensures that the forward-looking cost calculations for each network element reflect cost-causative principles to the greatest extent possible, and the non-account-specific costs are reflected in the prices of the various affected network elements in reasonable proportions.

In the case of expense-to-expense ACFs, total expenses are spread equally over all relevant expenses, ensuring that each ACF expense will be driven to the greatest extent possible to each product/service/element on a cost-causative basis.

Similarly, the calculations for the expense-to-revenue ACF spread expenses equally over all revenue to reflect cost-causative principles.

1. Network ACF

The Network ACFs are based on the jurisdiction-specific expenses incurred in the base year for repairing and rearranging plant and equipment, including the cost associated with responding to subscriber trouble reports ("R" dollars) and the cost

associated with moves, changes, rearrangements and upgrades to the network ("M" dollars). These expenses, which are captured by plant account, are divided by the jurisdiction-specific investments in the associated plant accounts to calculate the base Network ACF for each plant account. The network ACFs also include loadings to identify the overall administration, use, testing and operation of the network facilities used in providing service. These loadings have been categorized as either specific to central office assets, specific to outside plant assets, or general (*i.e.*, not specific to outside plant or central office plant accounts).

2. Wholesale Marketing ACF

The Wholesale Marketing factor represents the ratio between the wholesale marketing (product management and advertising) expenses and wholesale customer care expenses that will be incurred in a forward-looking wholesale environment, divided by revenue-producing investments. The advertising expenses that Verizon currently incurs are used as surrogate estimates for what Verizon would incur for advertising for wholesale services. These wholesale marketing expenses are divided by the revenue-producing investments in developing this portion of the Wholesale Marketing ACF. In addition, customer interfacing non-recurring revenue dollars are subtracted. Finally, the adjusted wholesale customer care expenses are divided by the revenue-producing investments to derive the customer care component of the Wholesale Marketing ACF. Verizon develops this ACF on a region-wide basis to reflect more accurately Verizon's organizational structure marketing to wholesale customers.

3. Other Support ACF

The Other Support ACF includes all support costs for information management, research and development, and procurement, as well as the capital and other costs associated with non-revenue-producing investments. The Other Support expenses are incurred in support of all classes of plant and are attributed to all revenue-producing investment categories. The recurring expenses associated with the non-revenue-producing investments are based on the information contained within Verizon's financial databases. These recurring costs are split between the Other Support ACF and Common Overhead ACF using an activity-based view of the functions. The recurring capital costs associated with the non-revenue-producing investments are determined by applying a capital-related ACF specific to each plant asset account. The factor is developed on a regional footprint basis.

4. Common Overhead ACF

Common overhead expenses are incurred in connection with General and Administration (G&A) functions, including the Executive, Planning, general accounting and finance, external relations, human resources, legal, and other G&A. Information management and corporate support costs are also included to the extent that those costs have not been reflected elsewhere. The Common Overhead ACF is the relationship between (a) Verizon-wide common overhead expense (adjusted to remove avoided retail costs) and (b) total Verizon expenses less common overhead expenses. In this manner (relating common expenses to element-specific or service-

specific expenses), the common overhead expenses are appropriately assigned to all categories of services, products and elements including non-recurring charges.

5. Gross Revenue Loading ACF

Gross Revenue Loading is a jurisdiction-specific factor that is applied against Verizon revenue to account for regulatory assessments and uncollectibles. Such expenses are associated with the level of revenues that Verizon actually receives. The regulatory commission assessments are identified directly from Verizon's financial databases. These dollars are divided by the total revenue for a given jurisdiction to derive the regulatory assessment component of the Gross Revenue Loading ACF. The uncollectible revenue component is calculated as the access and resale uncollectibles from Verizon's books, divided by the access and resale revenue from Verizon's books. This access and resale uncollectible component is used as an approximation of what is likely to be experienced in dealing with CLECs who purchase unbundled network elements.

6. Right-To-Use ACF

Right-to-use fees are the software costs that equipment manufacturers charge Verizon for the operation of and/or feature functionality associated with that equipment. Such software fees are capitalized based on recent changes in accounting rules. On March 4, 1998 the American Institute of Certified Public Accountants (AICPA) issued SOP 98-1, which recommended changes in the requirements for capitalization of software. As a result, effective January 1, 1999, the vast majority of software used for operating systems and applications in Verizon's network has been

capitalized. In Verizon's accounting system, the software is capitalized in the Intangible Asset Account 2690.

In the past, only a portion of Verizon's software costs were capitalized, such as the RTU fees associated with the initial purchase of the switch, and certain software that added new functionality to an existing switch; all other RTU costs associated with adding software to an existing switch were treated as expenses. With SOP 98-1, *all* switch software costs will be capitalized and booked to the Intangible Asset Account 2690, with the limited exception of software costs that are incurred specifically to fix a bug in previously installed software.

To reflect these accounting rule changes, Verizon has developed an RTU ACF. This ACF is based on a ratio of annual RTU software costs to total investment associated with either switching or digital circuit equipment. The costs are calculated as an amortization over the life of such software, based on budgeted expenditures over a planning cycle. The RTU ACF is applied to the appropriate investments throughout the cost studies.

C. GENERIC ADJUSTMENTS TO EXPENSE-RELATED ANNUAL COST FACTORS

Three types of adjustments are made generically to factors when adjustments are appropriate: (1) avoidance of any retail-related costs; (2) inflation/productivity considerations; and (3) a forward-looking-to-current conversion.

(1) Avoidance Of Retail-Related Costs. Any retail-only costs are directly excluded from the factor development. Where not directly identifiable, those

costs are approximated by the application of a retail avoided cost discount percentage. This avoided cost percentage is determined on the basis of an examination, by function, of each expense category to determine which, if any, particular expenses in each category are actually avoided when providing service on a wholesale/resale rather than a retail basis.

(2) Inflation/Productivity Considerations. Verizon's analysis of inflation and labor productivity is based on the trends that are observable for items such as negotiated unionized labor increases. Productivity and inflation are applied to the appropriate network, marketing and, other support expenses to account for anticipated changes in these costs over the study period.

(3) Forward-Looking-To-Current Conversion (FLC). ACFs are based on a relationship of a base period's expenses (after appropriate forward-looking adjustments) to investments, expenses or revenues. The FLC factor adjusts for the imbalance caused when an ACF is applied to a discounted TELRIC investment level.

D. CAPITAL-RELATED ANNUAL COST FACTORS

1. Depreciation ACF

Verizon utilizes a depreciation ACF in its forward-looking cost studies to reflect the appropriate economic lives of its forward-looking investments.

2. Return, Interest & Federal/State Income Tax ACF

The Return, Interest and Federal/State Income Tax ACF is calculated on the basis of book and tax depreciation and the return, interest and federal/state income tax requirements for each year of the plant asset's life. These results are then "pre-

sent worthed" over the life of the asset to the present, to ensure that no depreciation reserve deficiency is included in any of the plant accounts.

3. Other Tax ACF

The Other Tax ACF is used to calculate special franchise taxes, property taxes on the taxable plant, and other miscellaneous taxes imposed upon Verizon by the various taxing authorities (municipalities and counties) within a given jurisdiction.

E. Labor Rates

Labor rates are developed using data accumulated in the financial records of Verizon, from sources such as payroll records, personnel records, and time sheet reporting. Verizon's starting point for labor rate development is the basic wage expense for each Job Function Code (JFC),[3] divided by total productive hours for that JFC. Labor rates must also recover the costs associated with an employee's non-producing time for activities such as training, clerical support, and supervision, as well as for paid absence, premium time, payroll taxes and benefits. These expenses are distributed over productive hours to produce the total, directly-assigned labor cost per hour.

[3] The JFC is a code used to identify a specific type of work function, such as a Service Representative or a Central Office Technician. Productive hours are the time spent on a specific job function, such as provisioning trunks.

Labor rates are developed from the base year (or the most recent actual data available at the time that studies are conducted). The base year labor rates are trended forward using the Labor Trend factor, which is derived using projected annual salary increases and negotiated changes to labor contracts. The labor rates are then levelized over the planning period.

III. RECURRING COST STUDIES

A. THE LOOP

Verizon's cost studies address all loop types required by the FCC and offered by Verizon. These include various analog and digital loops as well as high capacity loops, subloops, and dark fiber. xDSL-compatible loops are not analyzed separately in the cost studies, because Verizon uses the appropriate two-wire or four-wire analog loop costs for xDSL-compatible loops.

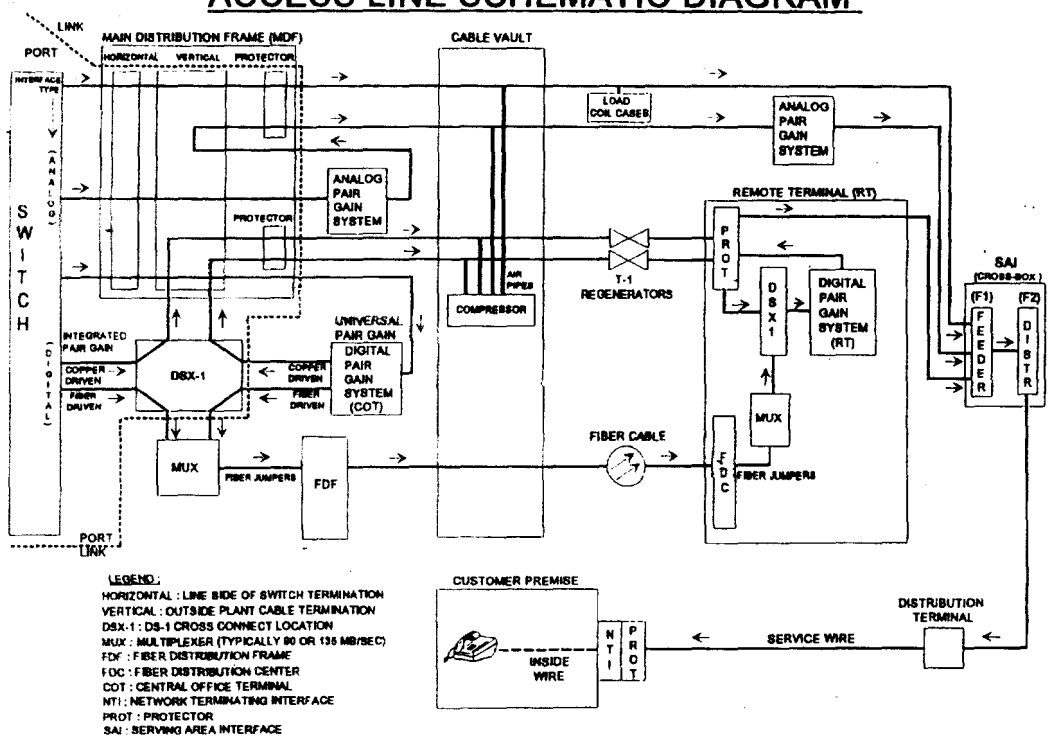
1. Costing Methodology

Verizon utilizes the Loop Cost Analysis Model (LCAM) to develop the investments and associated recurring costs of the loop; LCAM is discussed below.

2. Technical Construct

The diagram below represents the predominant components typically encountered in a loop currently in the network (not all of which are necessarily included in the forward-looking construct of a loop).

ACCESS LINE SCHEMATIC DIAGRAM



In the forward-looking network, a combination of fiber-fed DLC and copper cables are utilized to provide feeder facilities. (In some locations, the Company would use fiber to the building with a remote terminal located in the building.) The use of copper feeder is limited to those loops typically closer to the central office, while fiber-fed DLC is used beyond that point. This combined design strategy (using copper and fiber) eliminates costly network components required for longer loop copper designs (e.g., heavier gauge cables, load coils, repeaters).

When employing DLC, the infrastructure reflects the use of forward-looking digital loop carrier technology, in which the SONET-standard fiber transport is included with the digital carrier equipment. The specific design of the loop infrastructure, or "outside plant," depends on the demographic characteristics of the area.

3. Identification of Loop Investments

Loop investments include the following:

- Copper feeder, sub-feeder and distribution cable;
- Fiber optic feeder cable;
- RT equipment;
- Cross-boxes (SAIs/FDIs) and distribution terminals;
- Central office DLC termination electronics;
- Digital Cross-Connect Panels (DSXs) and (where utilized in connection with copper and/or universal interfaces) Main Distribution Frames (MDFs);
- Network Interface Devices (NIDs);[4] and
- Loop "structure" (*i.e.*, poles and conduits).

B. High Capacity Loops and Entrance Facilities

An entrance facility is a digital local access service that connects a CLEC's premises to a Verizon central office at the DS1, DS3, STS-1, OC3, and OC12 signaling rates. A high capacity loop connects a customer's premise to a Verizon central office. The cost studies are premised on the use of Synchronous Optical Network (SONET) transport equipment. This equipment is the most efficient technology currently available for provisioning high capacity local access service.

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[4] Although the NID is available as a separate unbundled network element it is also a component of the loop element. (For DS1 loops, a NID with additional functionality, sometimes referred to as a "smart jack," is required at the end user premises to support the isolation and testing and troubles reported by a CLEC to Verizon.)

Because of the unique nature of this service and the type of customer served, transport facilities are generally dedicated point-to-point facilities and are provided on a completely overlaid basis to the more general local access infrastructure. There is minimal opportunity for network resource sharing other than the fact that the fiber strands supporting this service and supporting the local access services addressed in the loop construct are usually contained in the same large fiber feeder cable from the central office to the customer location.

The relevant investments include:

- *Central office electronic equipment,* such as a multiplexer (Mux), digital cross connect frames, and fiber termination frames;

- *Equipment installed at the customer's premises,* such as a protective cabinet housing the Mux, power equipment, cross connect panels, and fiber termination frames; and

- *Fiber cable and associated "structure" investment,* assuming 100% fiber cable between the central office and the customer's premises.

C. xDSL-Compatible Loops

xDSL transmission technology can be utilized only over copper cables.[5] To these copper transmission paths, the CLECs can attach their own DSL electronics, adapted to the services that they intend to offer. Because the xDSL loops Verizon

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[5] Proposals for DSL-based services to customers served by loops with DLC systems are based on locating the DSL termination equipment (DSLAMs or related electronics) in the field, at the LECs' RTs, so that the DSL transmission still would be utilized only on the copper (distribution) portion of the loop, between the RT and the customer's premises. It would end at the RT, precisely where the DLC system — and the use of fiber as a transmission medium — begins. Signal transmission from the DSLAM to the ATM switch would use ATM packet protocols, not DSL technology.

provides (and has been asked to provide) use copper cables, the xDSL loop costs do not assume DLC. Instead, they are based on the two-wire and four-wire analog loop costs. In addition, non-recurring conditioning and related costs may be incurred.

D. DISTRIBUTION SUBLOOP

The Unbundled Subloop Arrangement (USLA) provides access to Verizon's metallic distribution pairs/facilities at the SAI/FDI. USLA provides a two- or four-wire transmission channel between a CLEC-provided Outside Plant Interconnection Cabinet (COPIC described below) and the NID or rate demarcation point at the end-user location.

USLA recurring costs include the costs of distribution facilities for two- and four-wire subloops, as well as the OSS implementation costs. The OSS implementation costs include the amortization of one-time expenses in connection with implementing the required Telcordia-provided OSS software for subloop unbundling (and its associated installation and testing).

E. UNBUNDLED FEEDER SUBLOOP

A feeder subloop provides a dedicated DS1 or DS3 two-point transmission path over a feeder facility in Verizon's network between a Verizon central office and a Collocation at the Remote Terminal (CRTEE) arrangement.

Unbundled feeder subloop recurring costs include the feeder facility costs associated with the subloops as well as the OSS implementation costs. The OSS implementation costs include the amortization of one-time expenses in connection with

implementing the required Telcordia-provided OSS software for subloop unbundling (and its associated installation and testing).

F. DARK FIBER

Dark Fiber consists of a continuous fiber optic strand within an installed fiber optic sheath that is owned by Verizon but is not connected to electronic equipment needed to power the line and transmit information. (Since information is transmitted on fiber optic cable in the form of light pulses, a fiber without the necessary electronics is appropriately described as "dark.") A CLEC that requests access to Dark Fiber is responsible for the establishment of any fiber optic transmission equipment or intermediate repeaters needed to utilize the fiber to transmit information.

The term "continuous fiber optic strand" refers to a fiber optic strand that does not require any splicing work in order to provide continuity between the CLEC's A and Z locations for the dark fiber circuit. The recurring costs associated with the provision of dark fiber include the costs of: (i) the fiber distribution frame termination (per fiber pair) and fiber jumper cable (per pair) at the customer's premises; (ii) the fiber cable itself and associated structure investment; and (iii) the central office fiber distribution frame (per fiber pair).

G. LOCAL AND TANDEM SWITCHING

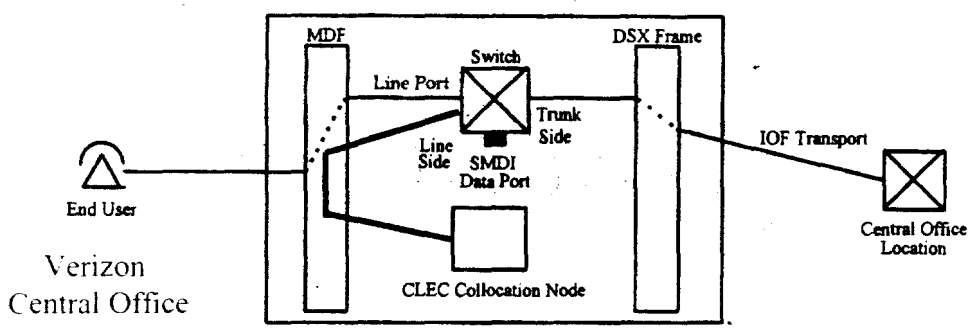
The Local Switching element consists of the following components:

- Line ports (analog, digital, and coin);
- Trunk ports (digital);
- Local switch usage (terminating and originating); and

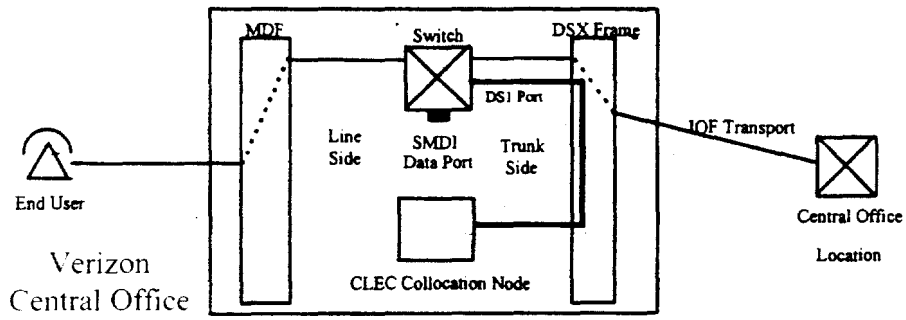
- Reciprocal Compensation Usage (terminating).

The simplistic diagrams below summarize the line and trunk port components.

Line and Trunk Port Components



Line and Trunk Port Components



All features that can be provisioned through the switch processor and that do not require any specific, unique hardware are included in the local switch usage element.

The tandem switching element consists of trunk ports (digital) and tandem switching usage. Trunk ports are either dedicated or common. Dedicated trunk ports are charged on a monthly basis, whereas common trunk port costs are charged on a "per minute of use" basis.

1. Costing Methodology

The Switching Cost Information System (SCIS) model, developed by Telcordia Technologies, estimates required investments in switching. The discounts that are used as an input to SCIS are based upon the discount that Verizon VA can actually receive when deploying switching equipment in the foreseeable future under its current vendor contracts. The discount is applied to the list price of the items in determining the appropriate investments.

2. Technology Assumptions

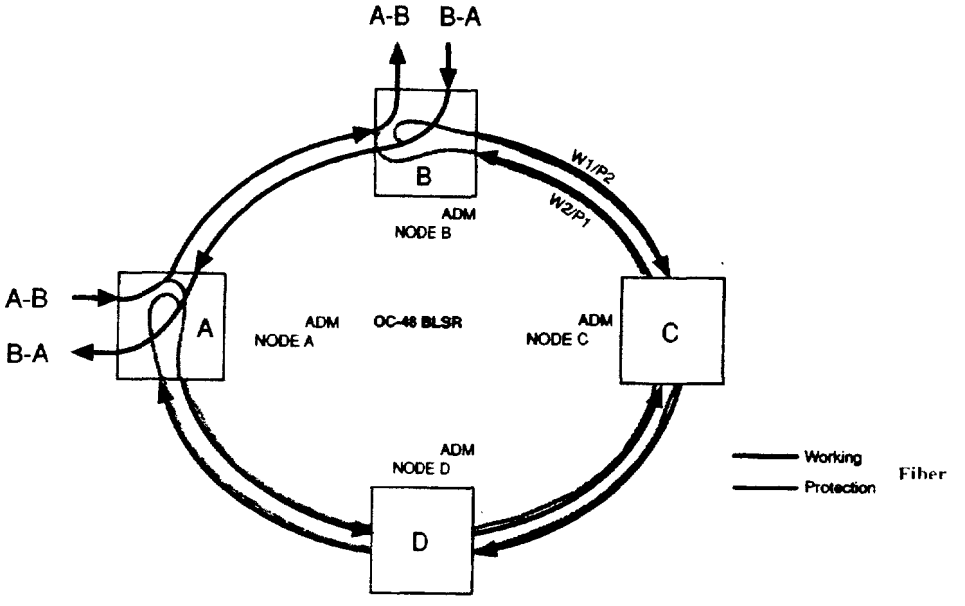
The forward-looking end-office switch construct is based on digital switching with a strategic mix of technologies. The lines are assumed to be provisioned on equipment consistent with the link forward-looking construct, including analog line units for copper or universal DLC loops and digital terminations for integrated DLC loops. Consistent with current FCC TELRIC rules, the study assumes current wire center (and, therefore, switch host/remote) locations.

H. INTEROFFICE (IOF) TRANSPORT

The Dedicated IOF element is defined to include IOF transmission facilities dedicated to a particular customer. Dedicated IOF is offered between Verizon-owned wire centers at the following signaling levels: DS1, DS3, STS-1, OC-3, and OC-12. Monthly costs are identified on a "fixed" basis and a "per mile" basis for each signaling level facility.

For simplifying illustrative purposes only, the diagram below represents a four node bi-directional line-switched ring.

Four Node Bi-Directional Line Switching Ring



The fixed investments are those identified at the originating and terminating Verizon wire centers, including electronic equipment such as SONET add/drop multiplexers (ADM), digital cross-connect systems (DCS), D4 channel banks and fiber terminations. The per mile investments are those that vary with the length of the facility and include interoffice fiber cables, structure, and any electronics at intermediate Verizon serving wire centers.

1. Cost Methodology

The Interoffice Facilities (IOF) Spreadsheet model is a set of interactive Excel worksheets that develop the UNE costs for dedicated interoffice facilities at all the required transmission levels. The model starts with current contract prices and information from vendors and engineering to determine the major equipment components of the circuit designs for IOF at the different transmission levels. The mate-

rial prices for the typical equipment configurations are compiled and investment loading factors (EF&I, power, land, buildings) are applied when appropriate to obtain the total installed cost. Annual cost factors are applied to the total installed investment. The resulting figure is then divided by 12 to obtain the monthly cost.

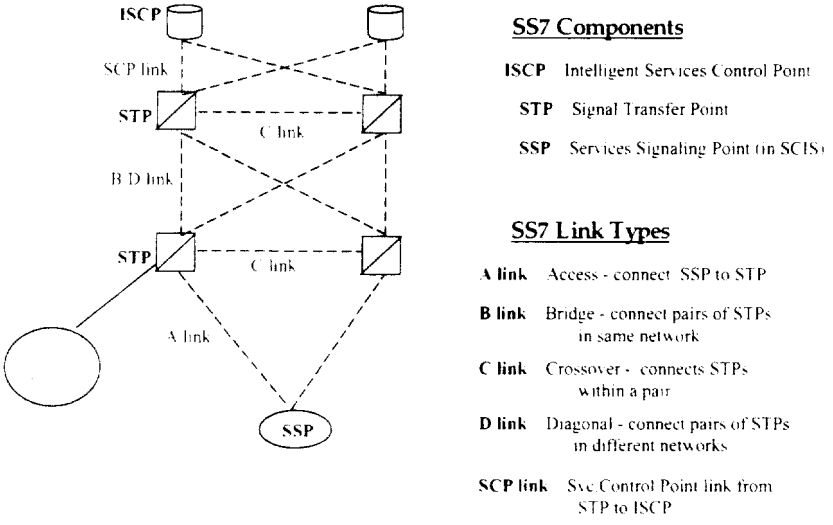
2. Technology Assumptions

Verizon uses SONET transport with 100% fiber facilities for all new growth applications in the interoffice network. Therefore the forward-looking assumption for the IOF is SONET transport with 100% fiber facilities. IOF Transport is based on facility models, which are schematics representing equipment routing using this construct. The facility models serve all signal levels (*e.g.*, DS1, DS3, STS-1, OC-3, and OC-12) throughout the Verizon IOF network..

I. SIGNALING SYSTEMS AND CALL-RELATED DATABASES

This signaling element includes the Signaling Transfer Points (STPs) Port, Signaling Links and access to certain databases.

SS7 Network Overview



Modern telecommunications networks transmit signaling information over communication paths separate from those used to transmit voice. Signaling information is switched at STPs, and is carried between STPs and local and tandem switches over signaling links. Routing and other information used by the signaling network is stored in call-related databases known as Intelligent Service Control Points (ISCPs). The protocol used for signaling information is known as Signaling System 7 (SS7). A call-related database query is a switch query and database response through the signaling network, which provides access to Verizon's Line Information Database (LIDB) and Toll Free Calling (800) database by means of physical access at the STP.

1. Costing Methodology

The material unit investments for the STP are developed using Telcordia's Common Channel Signaling Cost Information System (CCSCIS), based on the STPs' in-place configurations. The negotiated vendor discount is applied to the material investment in CCSCIS. Similarly, the material investments for the queries are developed using CCSCIS, based on the Next Generation Platform Intelligent Signaling Control Points (ISCPs) and negotiated vendor discounts.

2. Technology Assumptions

The construct used for the development of the cost of the STP port element reflects the actual configuration for a STP. This is determined by reviewing the actual STP network, the number of ports, and the forecasted future number of SS7 links. The unit costs are based on current link utilization levels and forecasted link demand. To develop the costs of the 800 and LIDB databases, a representative model of the ISCP for each database is determined and the forward-looking investments for that model are obtained through CCSCIS.

J. SMS

Service Management System (SMS) is a term coined by Bellcore (now known as Telcordia) for the Intelligent Network. Verizon's Advanced Intelligence Network (AIN) is a service platform that utilizes the SS7 signaling network and consists of a database that can intelligently route calls or provide other intelligent functionalities. The database is known as an Intelligent Service Control Point, or simply an AIN ISCP. The mechanism to query the ISCP is known as an AIN trigger and

occurs in an end office. End offices that have the ability to trigger are called Service Switching Points (SSP). This network element includes AIN Trigger, AIN Service Creation, AIN Query and AIN Record Storage.

K. LINE SHARING

Line sharing refers to the provisioning of xDSL-based service over the same physical loop facility used by the incumbent LEC for the provision of a retail voice grade service. As part of this arrangement, voice traffic is transported in the 0-4 KHz frequency range; data traffic is transported in the available spectrum above 4 KHz. Verizon is not assigning any additional loop costs to line sharing at this time. OSS costs required to support line sharing and testing costs (*i.e.*, the Wideband Testing System) are recovered as recurring costs on a monthly basis. The splitter installation charges are applicable if Verizon installs the splitter. Verizon also develops a monthly administrative and support cost for the splitter based on the placement of splitters (in the CLEC cage or on relay racks located in Verizon's central office space). Verizon also incurs non-recurring cross-connect costs. Non-recurring costs are developed for loop conditioning, where applicable, as well.

L. OPERATIONS SUPPORT SYSTEMS

The Access to OSS unbundled network element is defined by the FCC as consisting of five functions: pre-ordering, ordering, provisioning, maintenance and repair, and billing. These functions are defined as follows:

- **Pre-ordering**: the process whereby Verizon and CLECs exchange information about current and/or proposed customer products/services and/or unbundled network elements:

- **Ordering**: the process whereby a CLEC submits a request for products/services and/or unbundled network elements;

- **Provisioning**: the process whereby Verizon executes a request for a set of products/services and/or unbundled network elements and provides to the CLEC acknowledgment and status reports;

- **Maintenance and Repair**: the process by which a CLEC initiates a request for repair of existing products/services and/or unbundled network elements, with acknowledgments and status reports; and

- **Billing**: the process by which Verizon provides appropriate usage data to facilitate end-user billing. Billing also involves the exchange of information to process claims and adjustments.

Verizon has incurred significant costs as a result of the efforts to open the local exchange market to competition: one-time development costs for access to Verizon's operations support systems (OSS Access) and the associated recurring capital costs and ongoing maintenance expenses (*i.e.*, ongoing costs). The OSS developmental costs are associated with modifications to existing systems and development of new systems and interfaces necessary to provide competitors with access to Verizon's OSS, including the interface and gateway systems that UNE purchasers and resellers use to interact with Verizon for pre-ordering, ordering, maintenance, provisioning and billing, and the costs to modify Verizon's underlying core systems to accommodate these activities. The OSS modifications were addressed extensively as part of collaborative discussions among several state regulatory staffs, Verizon and its competitors. The development costs are based on the actual costs that were incurred, projected to a more recent time point using a combination of inflation and productivity adjustments.

The one-time up-front developmental costs fall into the following categories: (1) expenses associated with defining the methods and procedures for OSS access; (2) expenses associated with developing new system interfaces or gateways and functionalities; (3) expenses associated with modifying the underlying core systems to accommodate the new interfaces/gateways and functionalities; and (4) capitalized software costs incurred since the beginning of 1999 for interface/gateway/ functionality activity.[6] There also are recurring costs, ongoing software maintenance, and carrying costs related to the incremental investment necessary for such capabilities, functionalities and interfaces.

IV. NON-RECURRING COST STUDIES

Non-recurring costs are the one-time expenses associated with the activities necessary to process and provision a CLEC request for the initiation, change or disconnection (termination) of service. Non-recurring costs are generally incurred at the time the ordering, provisioning and termination of service occurs. These costs fall into four primary categories: (1) service order; (2) central office wiring; (3) provisioning; and (4) field installation. The non-recurring cost studies analyze the costs of all activities identified as necessary to respond to CLEC UNE requests.

The labor activities are performed in a number of functional organizations within Verizon. To develop these non-recurring costs, Verizon utilizes a forward-

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[6] These types of cost had previously been expensed but are now capitalized as a result of accounting

(Continued . . .)

looking estimate of the time required to perform each work activity involved in fulfilling a CLEC request and multiplies that time estimate by the appropriate labor rate. Labor rates are levelized over a three-year planning period. An allocation of common overhead expense and gross revenue loading are factored in as well.

Jurisdiction-specific labor rates are used where appropriate; in some cases the work may be performed outside the jurisdiction covered by the specific study, and then the jurisdiction or jurisdictions where the relevant work is performed are used.

V. COST MODELS AND COSTING TOOLS

A. VCOST

The VCost system is a cost study development environment. The purpose of this application is to provide an efficient and effective standard environment for developing, updating, and running cost studies. VCost is an integrated decision support spreadsheet building tool designed to develop consistent, high-quality cost studies in reduced cycle times. It is the result of a series of continuous improvement efforts initiated to refine the cost-development process utilizing a common look and feel as well as a consistent set of economic, engineering and computational assumptions. VCost facilitates development of new studies and study updates under differing sce-

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(Footnote continued)

reclassifications made pursuant to Statement of Position 98-1 (SOP 98-1) AICPA.